

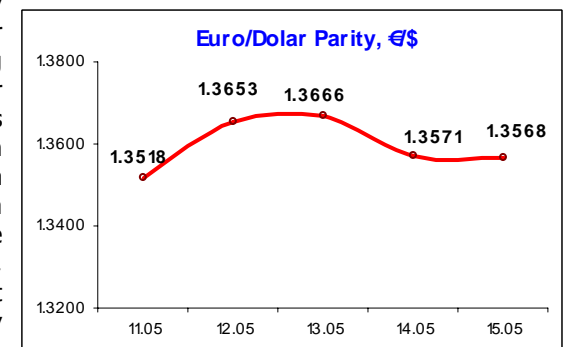
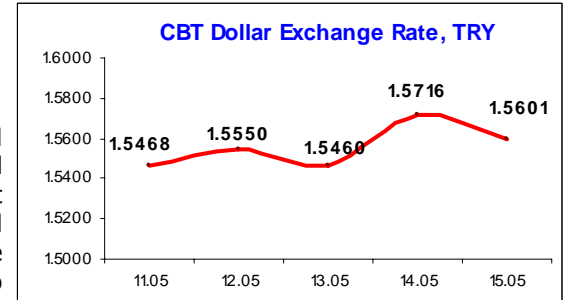
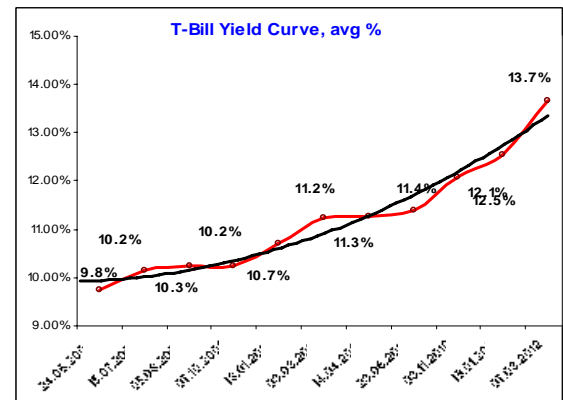
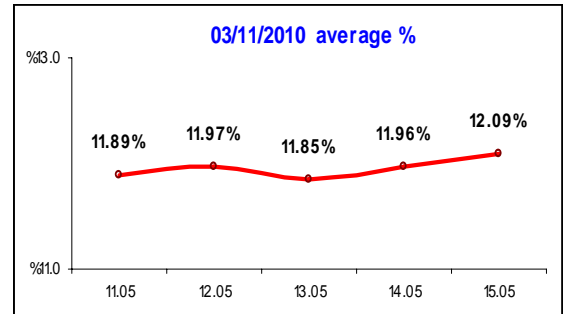
Weekly Bulletin

May 18-22, 2009

Focus of this week

- May-18** Council of Ministers
Meeting of Economic Coordination Council
CBT Governor Durmuş Yılmaz speaks, Seminar on "Global Crisis and Turkey"
Turkstat, Consumer Confidence, Apr
US, NAHB Home Price Index, May,
US Treasury Secretary Timothy Geithner's speech
- May-19** Atatürk Remembrance, Youth and Sports Day
US, Building Permits, Apr, cons: 530K, prev: 516K
US, Housing Starts, Apr, cons: 527K, prev: 510K
- May-20** Treasury, Central Government Debt Stock
US, FOMC Minutes of 29 April Meeting
US, Crude Inventories
- May-21** US, Philadelphia Fed, May, cons: -19, prev: -24.4
US, Leading Indicators, May, cons: 0.8%
US, Initial Claims, cons: 600K
- May-22** Bank of Japan Meeting
UK markets are closed, Bank Holiday tatili
CBT, Expectations Survet, May-II

STRATEGY: It took time for revision, but the political change was indeed important and rather massive for either 13 ministers have been removed from posts for good or their duties have been redefined. It is obvious that politically, and from the vantage point of implementing counter-cyclical economic policies, the composition of the college of ministers surrounding the Premier needed strong revision. While we expect the market response to remain almost negligible, the change is important. The ruling party headquarters may have conceived of the electoral trend as a bad omen for 2011, and taking precautions may have been seen as imperative. Calibrating the inner-party significance of the revisions is beyond our scope since neither we have knowledge of such issues nor do we intend to provide such clues here. Furthermore, any such hints may turn out to be false more often than not. However, we understand the AKP will not stand by observing a downward popularity trend to form. Hence, we expected until this week a carefully calibrated economic program to be rendered public along with the IMF agreement in late May. Now we are not that sure. In terms of equities, we do see no unexpected event occurring. This week is more likely to start with a downward move than not because Q1 banking financials were largely anticipated and priced in, and seconds because both the US and Asian equities dive down now. Our profit-taking expectation proved correct, but it came in with a delay.



Inflation %	Apr-09	Mar-09	12 month
PPI	0.65	0.29	-0.35
CPI	0.02	1.1	6.13

ECONOMICS: The CBT provided many a hint to the effect that inflation looks more subdued than it appeared to be in January and contraction is more pronounced. We gather that the O/N target rate may be cut down to c. 9% and be held constant for a while. Unless fiscal dominance prevents the CBT from easing further, and should the recession prove to be longer than anticipated, eating into 2010, the CBT would not hesitate to stage further rate cuts. We also would take this opportunity to conjecture that, measured in the American way, i.e. as percentage annualized change over the previous quarter GDP, seasonally adjusted, the Turkish GDP has been negative since Q2 2008. Hence, the first quarter of 2009 GDP growth will be fourth in a row if measured as suggested. We also take note on the claim that Q1 2009 GDP contraction might reach double-digit levels, a hint provided by the CBT last week. The 50 bps cut was in line with the consensus, and there has been no surprise there. We tend to think the CBT still sees risks are to the downside both on the inflation and growth fronts. Hence, we expected another moderate cut, i.e. 25 or 50 bps. The monetary policy council of the CBT did not signal any halt in its easing policy.

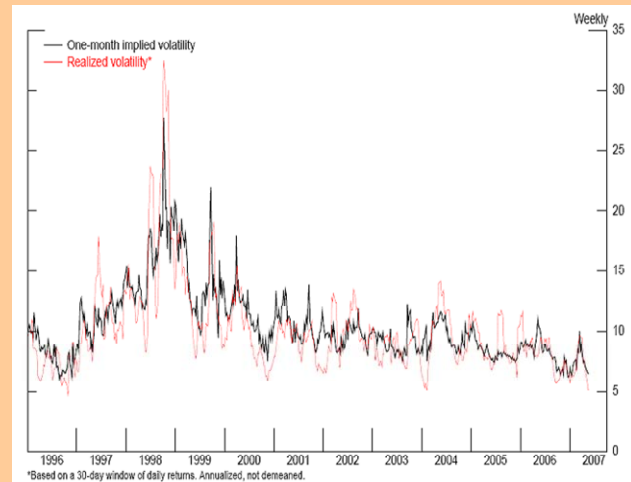
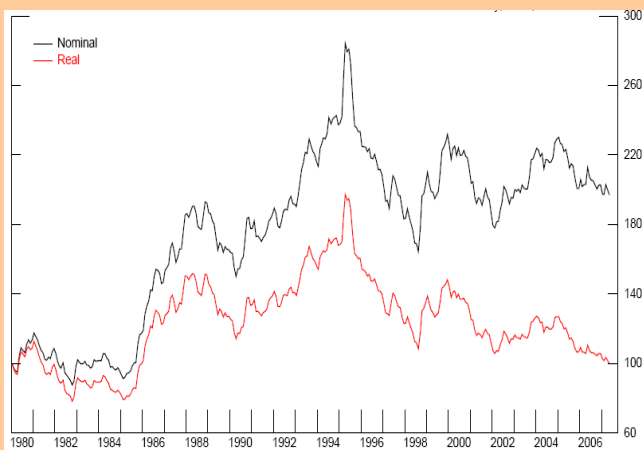
EQUITY: The markets extended the previously called six week rally to eight weeks as the index surged over 29,900 and 200-day moving average with rumours on Turkey's IMF deal and staggering bulls dominating US and global equities, not least the Asian markets. Tired of a continuing rise started on March 9, the ISE was flat in the band of 32,000-33,500 last week, trying to determine its new direction. Its Friday close was at its weekly high of 33.411, posting a weekly gain of 1.8%. In line with the dispersed negative sentiment in the US and Asian markets this morning we estimate selling pressure today. The ISE will probably test its support at 32,800. If the ISE-100 breaks this level down, we will follow the 32,000 for the rest of the week. For today, there have been no serious developments in the agenda, while the markets will continue to look for news related to the prolonged IMF agreement. The lack of a satisfactory explanation on the IMF side may increase the pessimism. Turkish markets will be closed tomorrow due to a Memorial of Ataturk and Youth Day, while the foreign markets will be under the effect of housing data in the US.

FIXED INCOME & CURRENCY: Interbank dollar quotations completed last week at 1.5640, after fluctuating between 1.5590-1.5740 on Friday. In the first trading of the week, opening at 1.5720, we expect USD/TL to float between 1.54-1.58, where EUR/USD parity lowered to 1.3460. Moving within 12.18%-12.03% in the last trading day of the week, benchmark compound rate closed at 12.04%. Starting today at 12.15%, we envisage benchmark bond rate to hover around 12.40%-12.00%.

May 2009– Monthly Domestic Debt Service (TRY mn)			
Date	To the Markets	Other	TOTAL
6-May	10,305	4,139	14,444
10-May	0	3,142	3,142
27-May	574	119	693
TOTAL	10,879	7,401	18,280

Gündüz Fındıkçioğlu, PhD

There are 3 episodes of yen appreciation widely attributed to the unwinding of yen carry trades. The most dramatic of these occurred in October 1998, immediately after the LTCM crisis, as many banks were reported to be cutting back on the leverage of their hedge fund clients. Two relatively recent periods that are commonly mentioned as periods of unwinding carry trades are those of May 2006 and February 2007, not to mention the post-Lehman episode. The Japanese real rate was at its 20-years low by the end of 2007. Vol charts do imply a large swing in both implied and realized vols in 1998, but not in 2006 and 2007.



A more systematic way to examine this asymmetry is to correlate the level of volatility with the change in the exchange rate. If yen appreciations are associated with higher volatility than yen depreciations, this correlation should be negative. Chart shows that implied volatility indeed is generally negatively correlated with changes in the dollar-yen exchange rate. However, measured realized volatility has little systematic correlation with the direction of exchange rate changes, perhaps because the skewness in the distribution of exchange rate movements owes to a relatively small number of tail events.

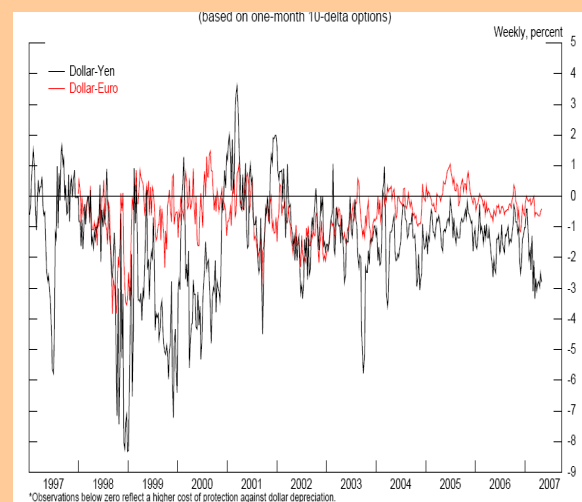
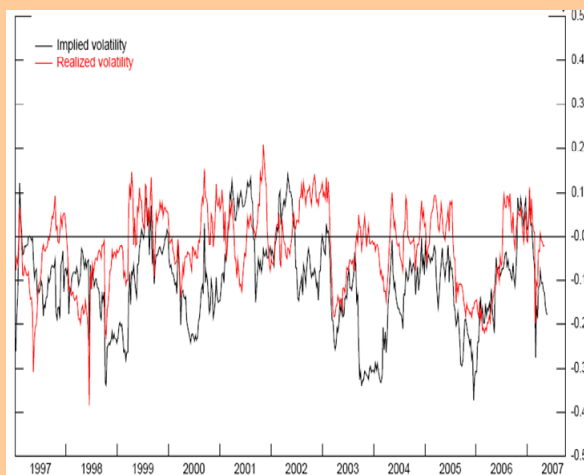


Chart shows risk reversals for dollar-yen and dollar-euro based on the differences in prices between significantly out-of-the-money call options and significantly out-of-the money put options. The risk reversal on dollar-euro is generally close to zero, consistent with a low level of carry trades in this currency pair. The risk reversal on yen was close to zero during the summer of 1998. The 1998 strong downward pressure on the yen was attributed to the carry trade. The price of protection against yen appreciation did not increase until after the yen appreciated sharply in early October, just when carry trades were supposedly unwinding. Risk reversal widened immediately after the yen appreciations of May 2006 and February 2007, but were not large prior to these dates when carry trades were building up. One interpretation of these results is that risk reversals reflect primarily the changing risk appetites or risk perceptions of market participants rather than changing shares of carry versus non-carry traders. **Prices peaked more for**

protection against yen appreciation than depreciation: that it may be the risk perceptions of the carry traders that are fluctuating most strongly.

Observers noted that in late February 2007, when the yen appreciated sharply, several high-interest-rate currencies depreciated significantly, including the Brazilian real and the New Zealand dollar. Such moves were, and still are, consistent with the unwinding of carry trades. Chart displays rolling 24-month correlations of dollar-yen with dollar-New Zealand dollar and dollar-Brazilian real. **The yen has been negatively correlated with these currencies recently, and the correlations also turned negative around October 1998, but the negative correlations around these three episodes are not large either in absolute terms or relative to other periods.** As data builds up, we ought to watch similar patterns emerge as the rewinding of carry trades may easily become the front page story of the months to come.

